UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF MONTANA

In re **SULA STORE, LLC,** Debtor.	Case No. **04-61901-11**

MEMORANDUM OF DECISION

At Butte in said District this 28th day of July, 2005.

In this Chapter 11 bankruptcy case, confirmation of the Debtor-in-Possession's ("DIP") Chapter 11 Plan of Reorganization, filed December 6, 2004 (the "Plan"), and the DIP's motion, filed January 18, 2005, for valuation of security of Atlantic National Trust, LLC ("Atlantic"), and Atlantic's objections thereto are pending. The Court held a hearing on these matters on May 5, 2005, and continued such hearing over to June 2, 2005. The DIP was represented at the hearing by attorney Harold V. Dye ("Dye"). Atlantic was represented by attorney Edward A. Murphy ("Murphy"). Licensed appraiser Tyler M. Jourdonnais ("Jourdonnais") testified at the May 5, 2005, hearing, and the appraisal which he prepared for Atlantic, Exhibit ("Ex.") A, was admitted into evidence over Atlantic's objection. At the hearing on June 2, 2005, the DIP's managing member John Kingsbury ("Kingsbury") testified, as did licensed appraiser Thomas G. Stevens ("Stevens"), and rebuttal witness – realtor Jim Risher ("Risher"). Stevens' Appraisal, Ex. C, was admitted. At the conclusion of the parties' cases-in-chief the Court closed the record and granted the parties 10 days to file simultaneous briefs, which have since been filed and reviewed by the

Court, together with the record and applicable law. The pending matters are ready for decision. For the reasons set forth below, a separate Order will be entered denying confirmation of DIP's Plan for failure to satisfy the "fair and equitable" requirement of 11 U.S.C. § 1129(b)(2)(A)(i)(II), and dismissing this case.

This Court has jurisdiction of this Chapter 11 bankruptcy under 28 U.S.C. § 1334(a). Confirmation of the DIP's Plan and DIP's motion for valuation of Atlantic's security are core proceedings under 28 U.S.C. § 157(b)(2)(B), (L) and (O). This memorandum includes the Court's findings of fact and conclusions of law. At issue is the valuation of Atlantic's security, and whether DIP's Plan satisfies the requirements of § 1129(b)(2)(A)(i)(II) with respect to the value of Atlantic's interest in the estate's interest in Atlantic's security.

The ballot report shows and the Court finds that the only ballots submitted, by Farmers State Bank (Class 3.4) and Kurt and Deborah Thomas (Class 3.6), accepted DIP's Plan. No ballots were submitted rejecting DIP's Plan, although Atlantic objected to confirmation and is deemed to have rejected the Plan for its Class 3.5. By virtue of the ballots for Classes 3.4 and 3.6, the Court concludes that at least one class of impaired claims, has accepted the plan in satisfaction of 11 U.S.C. § 1129(a)(10).

FACTS

Kingsbury is 69 years old and managing member of the DIP, which owns and operates under the dba "Sula Country Store & Resort" – a business consisting of a general store, gas station, RV campground with cabins and cottages available for rent, and a restaurant. Kingsbury testified he is an experienced accountant who started working in the hospitality industry in 1954 and has worked for several hotels and casinos. He testified the Debtor purchased 3.27 acres of

real property located at 7060 Highway 93 South in Sula, Ravalli County, Montana[1] (hereinafter the "Sula Store property"), in 1998. Debtor financed the purchase with a loan from Farmers State Bank. Ex. A, p. 6, states the purchase price Debtor paid was $450,000.

Kingsbury testified that the Debtor did not anticipate having to replace the septic, water or electrical systems for the Sula Store property, but that such improvements became necessary and were made. The Debtor took out another loan for construction purposes from an entity Kingsbury identified as MCDC. The construction loan was guaranteed by the United States Small Business Administration ("SBA") and apparently[2] secured by the Sula Store property. Kingsbury testified the MCDC loan was subsequently transferred to Atlantic. Ex. A., p. 6, states that an estimated $500,000 was expended on the Sula Store property to expand the store, replace gas pumps, islands and underground storage tanks, other maintenance and improvements. Kingsbury testified that the work finished and the Debtor began operations in August of 1999.

For the first 5 years the Sula Store operated as a KOA franchise. The Sula Store operated until August of 2000, when Kingsbury testified a fire effectively ended their season. In 2001 and 2002, he testified, highway construction wiped out both of the Debtor's summer seasons, and in 2003 another fire year wiped out their business. See, Ex. A, p.7.

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[1]There is a discrepancy in the Section number in the legal description of the property. Schedule A lists the description as a portion of the NE1/4 of Section 12, Township 1 North, Range 19 West, P.M.M., Ravalli County, Montana, also described as Parcel 1, Certificate of Survey ("COS") No. 4386. Stevens' appraisal, Ex. C, describes the tract as located in the NE1/4 of Section 17, Township 1 North, Range 19 West, and COS #4386. Ex. A, Jourdonnais's appraisal, lists the tract as a portion of the NE1/4 S17/T1N/R19W, Ravalli County – Parcel 1 COS #4386.

[2]The security documents for the construction loan and Atlantic's claim were not offered, and are not part of the record.

Kingsbury testified that the Debtor acquired 4 cabins and cottages for rental business, but that the cabins are for sleeping only, and have electricity but lack bathrooms or water, except at a common bathhouse. The cottages have bathrooms, kitchens water and power. Kingsbury testified that the cabins and cottages all rest on skids, and as such are considered furniture, fixtures and equipment ("FF&E"), not real property. On cross examination he explained that the cabins and cottages rest on cinder blocks, which are dug into the ground only to the extend required to make them level, and that the cabins and cottages are not attached to the cinder blocks other than by gravity. Kingsbury admitted that the bare ground under the cabins and cottages could be used for RV rental space, but he testified that RV rental is only a 6-month business and could not produce as much income as the cabins and cottages, which rent year round.

Kingsbury testified that, because of the loss of business from fires and highway construction, the only "normal" period the Debtor has experienced for RV rental was from August 1999 through July 2000, during which the occupancy rate for the summer months was 75%, but barely reached 5% for the other 9 months, an average Kingsbury testified worked out to 13% per month. However, DIP's Ex. A noted that the period from 1998 through 2000, which includes Kingsbury's "normal" rental period, was a period of construction and remodeling, including the discovery and designation of the site as "contaminated" by the Montana Department of Environmental Quality ("DEQ") from overspills into underground storage tanks, and removal of contaminated soil. Ex. A, pp. 6-7.

The Debtor filed a Chapter 11 bankruptcy petition on June 18, 2004, and filed its Schedules and Statements on June 23, 2004, listing assets valued at $736,430 and total debts of

$951,778. Schedule A lists the Sula Store property as having a current market value of $500,000, as Kingsbury testified, encumbered by secured claims totaling $693,228. Schedule B lists personal property totaling $236,430, including cabins and cottages valued at $100,000, business equipment valued at $31,000, and $83,003 in inventory. The only other FF&E listed on Schedule B are an ATM machine ($2,668), spa and equipment ($7,500) and water iron filter ($378).

Schedule D lists secured creditors, including Atlantic which is scheduled as having a claim in the amount of $291,983 secured by a second lien on residence, followed by the Sula Store property description, with "0.00" listed as the unsecured portion of Atlantic's claim. The DIP did not mark Atlantic's secured claim as disputed, contingent or unliquidated[3]. Other relevant secured claims listed on Schedule D are Deborah Thomas with a claim of $95,647 secured by cabins and cottages; Farmers State Bank with two (2) secured claims – $50,000 secured by "FF&E Inventory" valued at $0.00 and $386,140 secured by a first mortgage on the Sula Store property; and Ravalli County Treasurer with a lien on the Sula Store property in the sum of $15,105. The Statement of Financial Affairs lists the Debtor's income from business in fiscal year 2002 as $590,822; in 2003 as $560,036, and $182,910 to the date of filing in 2004.

The 11 U.S.C. § 341(a) meeting of creditors was held on July 14, 2004. The § 341(a) notice included a claims bar date of October 12, 2004, and was mailed to Atlantic and other creditors.

Farmers State Bank filed Proofs of Claim Nos. 5 and 6 on September 17, 2004. Proof of

[3]None of the secured claims are listed on Schedule D as disputed, contingent or unliquidated.

Claim No. 5 asserts a claim in the amount of $387,068.00, secured by promissory note, trust indenture and security agreements dated 1998 and later modified[4]. That claim of Farmers State Bank is secured by real estate, fixtures, equipment and a liquor license with a total value stated of $736,430. Proof of Claim No. 6 is filed as a secured claim in the amount of $49,219.22 secured by equipment, fixtures, and liquor license valued at $236,430.

Atlantic did not file a proof of claim. DIP's attorney Dye filed Proof of Claim No. 8 on behalf on Atlantic pursuant to F.R.B.P. 3004 on December 1, 2004, stating a total claim in the amount of $291,983.00, of which $94,576.71 is listed as a secured claim at part number 4 but as an *unsecured* nonpriority claim at part number 6. Proof of Claim No. 8 asserts at part number 5 that Atlantic's claim is secured by real estate, and it states the "Value of Collateral" is "$0.00" and the arrearage included in the secured claim is $97,576.71. Atlantic moved to strike Proof of Claim No. 8 filed by the DIP on its behalf. The Court denied Atlantic's motion to strike, but noted in its Order[5] that Dye admitted at hearing that Atlantic is not bound by Proof of Claim No. 8.

DIP filed its Chapter 11 Plan of Reorganization and Disclosure Statement on December 6, 2004. The DIP's Plan lists Atlantic as having an impaired secured claim, sub-classified in Class 3.5, and secured by a second trust indenture on real estate. Advanta Bank Corp. and Farmers State Bank[6] are classified as unimpaired claims. The Plan and Disclosure Statement

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[4]The amounts stated on Farmers State Bank's claim do not include any attorney's fees under 11 U.S.C. § 506(b).

[5]Docket no. 33 entered February 11, 2005.

[6]For Class 3.2 representing Farmers State Bank's operating loan, Proof of Claim No. 6.

describe Atlantic's claim as undersecured, and the Plan proposes at Article III to pay Atlantic in full without interest over 25 years if Atlantic makes an 11 U.S.C. § 1111(b) election[7], or if no election is made to pay Atlantic's allowed secured claim over 20 years "with nominal annual payments calculated by level amortization with interest at the rate of the prime in effect on the effective date plus 1.25 percent" and subject to adjustment every 5 years. The Plan proposes to pay unsecured claims at least 50% of their allowed claims[8], with Kingsburys to retain their equity interests. The Plan is to be funded from the DIP's continuing business operations.

The "nominal annual payments" the Plan proposes to make to Atlantic are adjusted downward at Article IV of the Plan by a declining percentage until 2008 in "order to restore working capital". Article V limits the period for annual payments to be made to the season from June through October. Article VIII at page 7 includes treatment of contingent, disputed, unliquidated and unfiled claims and states: "Any creditor which does not agree with the amount that his claim is listed in Debtor's schedules who does not file a claim by the fist [sic] date set for hearing on confirmation of the plan will be paid only the amount shown on the schedules plus such interest as is provided for in this plan."

The Disclosure Statement includes an attachment setting forth cash flow projections through 2010, including the DIP's assumptions that gross sales and cost of goods sold each will increase at the rate of 7% per year, while operating expenses will increase at a rate of 3%. The

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[7]The record does not reflect that Atlantic made a § 1111(b) election.

[8]For Class 5.2, nonpriority, unsecured claims of more than $1,000 who do not elect to reduce their claims to $1,000 to join Class 5.1 for full payment. Plan, pp. 3, 5, Articles I, III.

attached income statement for year 2003 shows a $9,212 net loss after deducting expenses[9] from a gross profit of $224,209 on sales of $521,329. The cash flow projections attached to the Disclosure Statement show a $240,000 gross profit in year 2004 on sales of $600,000, with $56,000 net income before depreciation and debt service after deducting expenses, including a $42,000 annual draw for the DIP's members through year 2010. The remaining annual net income projections shown are $68,540 for 2005; $82,128 for 2006; $96,843 for 2007; $112,769 for 2008; $129,995 for 2009; and $148,620 for 2010. Projected annual payments to Atlantic on its impaired secured claim, stated as $291,983, are $7,700[10] in 2005; $8,800 in 2006; $9,900 in 2007; $11,000 in 2008; and $12,100 in 2009 and thereafter, which over 20 years totals $231,000.

The DIP filed a motion for valuation of Atlantic's security on January 18, 2005, seeking to value Atlantic's security at $500,000 and fix Atlantic's allowed secured claim in the amount of $94,546.71[11]. Atlantic filed an objection alleging its collateral is worth $832,000 and that it is fully secured. Atlantic also filed objections to approval of the Disclosure Statement arguing the DIP failed to follow proper procedure for lien stripping and valuation, lack of financial information for 2004, and lack of discussion about the various creditors' collateral. After hearing

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[9]The 2003 financial statement expenses do not reflect the annual members' draw of $42,000 included in the cash flow projections. There is a "Payroll and Related" charge of $23,909 reflected in the 2003 total expenses, which are stated in the amount of $160,990. The 2004 projected cash flow lists operating expenses of $142,000 separate from the $42,000 members' draw. There is no explanation how expenses were reduced so dramatically in contrast to the DIP's statement that operating expenses would increase by 3% annually.

[10]After reduction of the "nominal interest payment" to replenish working capital. Art. IV of DIP's Plan, p. 5.

[11]DIP arrived at the $94,546.71 net value by subtracting prior liens of $405,453.29 (presumably the sum of Farmers State Bank's claim secured by real estate – Proof of Claim No. 5, and the tax claim of Ravalli County Treasurer) from DIP's asserted value of $500,000.

the Court sustained Atlantic's objection and ordered the DIP to supplement the Disclosure Statement, which DIP did on January 25, 2005, including a financial statement for year 2004.

DIP's supplement explains that its asserted $500,000 value of the Sula Store real property is based on Kingsbury's opinion, which in turn is influenced by an appraisal of the property prepared for Atlantic[12]. The attached 2004 financial statement lists $933,143 in fixed assets including land ($50,000), improvements ($24,500), buildings ($215,000), cabins and cottages ($90,296), FF&E ($31,000) and "new construction" ($522,347). The 2004 financial statement further states 2004 gross sales at $568,297, with a net operating profit of $65,550 after expenses. Debt service, depreciation and interest expense is stated as $65,543, leaving a net profit of $7 without regard to the $42,000 annual members draw from the DIP's cash flow projections, which is not included. The amended Disclosure Statement was approved by Order entered February 14, 2005, which set the hearing on confirmation of DIP's Plan for March 10, 2005, the same date set for DIP's motion for valuation of Atlantic's security.

Atlantic filed objections to confirmation on the grounds DIP's plan fails to provide for its allowed secured claim by payments of a value of at least the value of its interest in the estate's interest in the Sula Store property as required under § 1129(b)(2)(A); that the cabins and cottages are fixtures and improvements subject to Atlantic's lien ahead of Deborah Thomas; and that the Plan violates the absolute priority rule of 11 U.S.C. § 1129(b)(2)(B)(ii). On March 9, 2005, and again on March 29, 2005, the DIP and Atlantic jointly moved to continue the hearing on the grounds Stevens' appraisal was not complete. The Court continued the hearing until May 5,

[12]It does not state which appraisal, but it can be assumed Kingsbury relies on the appraisal prepared by Jourdonnais, Ex. A.

2005, when Jourdannais testified and Ex. A was admitted.

On June 2, 2005, Kingsbury testified that in his opinion the value of the Debtor's real estate is $500,000. Notwithstanding DIP's supplement to its Disclosure Statement stating that Kingsbury's opinion is based on the appraisal prepared for Atlantic, Kingsbury criticized the Jourdonnais appraisal value of $550,000 because he claimed it includes projected income from the 4 cabins and cottages, which he testified are FF&E because they are on skids or cinder blocks and not part of Atlantic's security. Kingsbury's testimony is not supported by Jourdonnais' appraisal on which he relied.

A. Jourdonnais Appraisal – Ex. A

Jourdonnais is a commercial real estate appraiser with 17 years experience, licensed in Montana, Arizona, and Nevada, who performed an appraisal of the Sula Store property for Atlantic. Ex. A is Jourdonnais' appraisal for the Debtor's real estate only, which as his cover letter to Ex. A explains means land and permanent buildings, and not FF&E[13] or going concern business value. Jourdonnais admitted that he did not attempt to value the Debtor's business, and repeatedly states the 4 mobile rental cabins are not included in his valuation of the property. Ex. A, pp. 6, 25, 31. Gas pumps and canopy are not part of Ex. A's appraisal value. P. 25.

Jourdonnais placed a market value for the land and permanent buildings "as is" at $550,000 as of March 25, 2004, assuming the subject property is free and clear of any environmental contamination and meets the State of Montana Department of Environmental Quality ("DEQ") standards. Jourdonnais noted that taxes for the years 2000-2003 in the amount

[13]Jourdonnais testified that he asked Kingsbury for lists of business FF&E but Kingsbury did not provide any, which comports with Ex. A.

of $12,703.40 plus penalties and accruing interest were delinquent, and estimated the marketing period for the subject property at 12 months, or less.

Ex. A, p. 38 lists the $550,000 value arrived by Jourdonnais as made via the Sales Comparison Approach, with a value range from comparable sales of between $469,600 to $600,000. The Income Capitalization Approach, using a 12.0% capitalization rate on potential effective gross income of $148,650 less $82,131 expenses ($66,519), yielded a market value of $554,325 which Jourdonnais rounded to $555,000 value. Ex. A, p. 44. Jourdonnais did not employ the Cost Approach. He concluded that the "as is" market value of the Sula Store real estate was $550,000 as of March 25, 2004. Ex. A, p. 45. Jourdonnais adjusted comparable sales as escalating at the rate of 5% per annum. Ex. A, p. 36. Since Ex. A was dated more than a year before the first date of the confirmation hearing, according to Jourdonnais 5% annually must be added to his $550,000 value estimate to bring Jourdonnais' appraised value up to date, resulting in a value according to Jourdonnais' appraisal as of May 2005 of more than $577,500[14].

Stevens was questioned about Jourdonnais' appraisal and enumerated 3 problems: First, that Ex. A was outdated because it was a year old and the valuation was effective as of March 25, 2004; second, that Jourdonnais based Ex. C on plans and specifications for renovation and not on the property's then-current condition; and third, that in Stevens' opinion Jourdonnais did not consider certain assets in Ex. A.

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[14]The confirmation hearing commenced more than 13 months after the effective date of Jourdonnais' appraisal of March 25, 2004. Adding 5% to $550,000 results in a value on March 25, 2005, of $577,500. This adjustment must be made because the valuation of collateral for purposes of fixing a claim must be at or near the time of confirmation. *In re Barnes*, 14 Mont. B.R. 187, 190-91 (Bankr. D. Mont. 1995); *In re Rivers*, 10 Mont. B.R. 210, 211 (Bankr. D. Mont. 1991).

B. Stevens Appraisal – Ex. C.

Stevens is an MAI appraiser licensed first licensed in 1980. He testified that he has been a real estate appraiser for 30 years and performs at least 2 appraisals of convenience stores each year. On cross examination Stevens admitted that, originally, he did not understand that he was to testify as to his conclusions in this case, and he did not recall when he first learned he would be called to testify. Stevens testified that in performing his appraisal he was given the property's legal description, Debtor's tax returns and income and expense statement. Stevens researched the real estate taxes and performed an on-site visit.

The valuation of the DIP's property arrived at by Stevens on Ex. C is dated March 1, 2005. The cover letter to Ex. C dated May 3, 2005, acknowledges that the cabins and cottages are on skids and not permanent foundations, and are considered personal property not included in the overall value.

Stevens analyzed the Sula Store property's current market value using three valuation approaches: Cost, Income Capitalization and Sales Comparison. Each method is discussed in Ex. C, and Stevens testified as to each method at trial.

In determining the value by the Cost Approach Stevens examined 3 comparable sales of real property on Highway 93 located north and south of the Sula Store, with relevant adjustments for size, zoning, and amenities such as river frontage to determine the value of the land and improvements. Stevens arrived at a value per acre of $45,000 and $150,000 total value for the real estate, plus improvements and additions raising the Cost Approach value to $650,000. Ex. C, pp. 15-17. On cross examination Dye asked Stevens about the $150,000 value assigned to tank, canopy and pumps, suggesting that those assets were fixtures and security to a lender other

than Atlantic. Stevens replied that he did not take into consideration which creditor was secured by which assets. In any event, Ex. C states that Stevens assigned the least weight to the Cost Approach in arriving at his valuation.

The Income Capitalization Approach determined the present worth of future income-producing capabilities of the Sula Store, building rental, RV space rental for 29 RV spaces[15] totaling $119,182 effective gross income, less $31,643 expenses for pre-tax net income of $87,539, to which Stevens applied a 12.5% capitalization rate ("cap rate") and arrived at a value of $700,000. Ex. C, pp. 18-20. On cross examination Stevens admitted that a reduction of his estimated 35% RV occupancy rate to 15% would reduce the effective gross income, but Stevens testified he reached his 35% estimated occupancy rate after speaking with RV campground operators and realtors, in addition to Kingsbury. Dye questioned Stevens about the $11,918 management expense, to which Stevens replied that the business needs intensive management only 4 months out of the year[16] which an investor could obtain for $12,000.

For the Sales Comparison Approach Stevens looked at 4 comparable sales, 3 of which are located in the Bitterroot Valley like the Sula Store[17]. Stevens located the 4 comparable sales using the Bitterroot and Missoula Multiple Listing Services, after which he contacted a realtor.

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[15]Ex. C, p. 19, notes that the 10 cabin/cottage spaces are included among the 29 RV spaces, 11 of which have full hookups and 18 with only electricity and water. Stevens testified that he relied on what Kingsbury told him regarding the utility hookups for the cabins and cottages.

[16]This short season is corroborated at page 6, Article V of DIP's Plan, where DIP states that all but 5% of the DIP's annual payment is generated by revenues over 4 months.

[17]The comparable sale not located in the Bitterroot Valley is sale No. 5 located in St. Regis, which took place in August 2003. Ex. C, p. 22. Stevens testified that he chose it as a comparable sale because of its amenities, including laundry, swimming pool and a home.

Two of the comparable sales, 1 in Victor and 1 in Corvallis, involved convenience stores and were used to obtain a value per square foot of Sula Store building area, and the other 2 sales in Hamilton and St. Regis were sales of camping and RV properties to obtain value of each camp/RV space[18]. Stevens admitted that land value generally decreases as distance from urban areas increases, but not the value of improvements.

Ex. C, p. 14 employed an overall appreciation rate of 10% per year for the comparable sales compared to the 5% used by Jourdonnais. The comparable sales were of differing size, location and conditions, and to correlate the comparable sales Stevens adjusted them for age, condition, quality and inflation, arriving at a square footage value for the Sula Store store building of $200, and RV site value of $4,000/site. Stevens concluded that the Sales Comparison Approach value of the Sula Store real property is $670,000. Ex. C, pp. 21-23.

On cross examination Dye questioned Stevens about the $4,000 per RV site value he utilized under the Sales Approach, versus the $3,005 per site value used under the Cost Approach, Ex. C, p. 15. Stevens replied that the $3,005/site value under the Cost Approach does not include the value of the other amenities such as driveways, water well, septic and shower which are reflected in the $4,000/site value under the Sales Approach. Dye asked about the same contrast between the $399,200 convenience store value under the Sales Approach, Ex. C, p. 23, versus the $275,141 value of total building improvements under the Cost Approach, Ex. C, p. 16. Stevens testified that the same answer applies: The $200 per square foot value under the Sales Approach is the gross value including all the other amenities, while the Cost Approach value of

[18]On cross examination Stevens testified that the RV campground comparable sales were listed as having stores, but he found that the facilities were not really stores.

the building improvements does not include the other amenities.

From the Debtor's federal tax returns for 1999 through 2003, Stevens determined an average income from the real estate and business enterprise of $97,000 per year from which $43,000 is attributable to the business enterprise and $54,000 from return on real estate. Stevens applied a cap rate of 25% of the $43,000 to arrive at a business enterprise value of $172,000 rounded to $170,000. Ex. C, p. 24.

Reconciling the valuations arrived at by the 3 approaches, Stevens gave the Cost Approach the least weight. Stevens concluded that as of March 1, 2005, that the Sula Store real estate had a market value of $675,000. Ex. C, p. 26. Stevens attributed an additional $170,000 to the value of the business enterprise. Ex. C, pp. 26, 28.

C. Rebuttal Evidence – Chalet Bearmouth Sale.

The DIP called realtor Jim Risher to testify on rebuttal. Risher testified that he has been a realtor for 14 or 15 years, is a member of local multiple listing services, and that he sold the Sula Store property to the Debtor. Risher testified that he takes continuing education classes on the valuation of property, and that he knows how to value property including his specialty – hospitality property. However, he admitted he is not licensed or certified as a real estate appraiser.

Risher testified about a comparable sale of a bar and RV campground at the Bearmouth area north of Interstate 90, Granite County, Montana, known as "Chalet Bearmouth", which is not included among the comparable sales referenced in Stevens' appraisal, Ex. C[19]. The DIP offered a copy of multiple listing data as Ex. B, but the Court sustained Atlantic's objection and

[19]The Bearmouth Exit off I-90 is shown on the map at Ex. C, between pages 21 and 22.

refused admission of Ex. B on grounds of hearsay and lack of relevance . The DIP thereafter made an offer of proof for the record, arguing that inclusion of Ex. B shows Stevens' bias by omitting the Chalet Bearmouth comparable sale from Ex. C.

The Court allowed Risher to testify about the Chalet Bearmouth sale, ruling that his testimony goes to the weight of the evidence. He testified that he looked at the Chalet Bearmouth property a few years ago, and the MLS listing data. Risher also showed the Chalet Bearmouth when it was listed by a realtor other that the realtor who eventually closed the sale. He testified that the Chalet Bearmouth has had 3 owners in the last 10 years, and that in his opinion it is very comparable to the Sula Store property because it is located on a river off a major highway, and has a campground and a store[20]. In addition Risher testified that Chalet Bearmouth has a Montana all-beverage liquor license, a large restaurant and is larger than 180 acres. Risher testified that Chalet Bearmouth sold for $384,000 on June 24, 2004.

D. Court's Finding of Value of the Sula Store Property.

Based upon the reasoning set forth below, this Court finds and concludes that the value of the Sula Store property is $605,000.00.

CONTENTIONS OF THE PARTIES

The DIP argues that Kingsbury's $500,000 value opinion can be reconciled with Ex. A's $550,000 value from Jourdonnais because Ex. A includes the value of cabins and cottages which are not affixed to the real property and are collateral for other creditors. DIP attacks Stevens' appraisal as "made as instructed" for Atlantic, and contends that Stevens lacks credibility and Ex.

[20]The Court notes that the Chalet Bearmouth property is located on a different highway, next to a different river, in a different valley and a different County than the Sula Store.

C is full of inconsistencies and unwarranted adjustments and assumptions with respect to Stevens' $45,000 per acre land value, the $150,000 assigned to gasoline tanks, canopy and pumps which are trade fixtures and security for Farmers State Bank, overhead and profit, and occupancy rate. DIP contends that Stevens' use of the Sales Comparison Approach valued the Sula Store property and improvements much higher than 2 larger RV courts with similar improvements, ignored the stores on both RV comparable sales, valued the RV sites 25% higher than the cost to construct new RV sites and valued the store much higher than the cost to construct a new store, notwithstanding 25% annual depreciation. DIP submits that Stevens appraisal was not an honest valuation opinion but rather a "bought and paid for" opinion to support's Atlantic's litigation position, and that Stevens therefore is not credible and his testimony should be given no weight.

Atlantic argues that the DIP may not strip its lien simply by filing a proof of claim for Atlantic, and that even using Kingsbury's $500,000 Atlantic has a secured claim in the amount of at least $112,932 which is not provided for in the DIP's Plan. Atlantic argues that under case law construing 11 U.S.C. § 506(a), where debtor proposes a plan retaining collateral the property should receive a going concern rather than liquidation value, and the valuation should be determined as of the effective date of the plan, and thus Ex. A is outdated by more than a year. Atlantic argues that Ex. A fails to provide a going concern value and should not be used. Instead Atlantic urges the Court to adopt Stevens' $845,000 land and business value on Ex. C based on the DIP's intended use in the Plan. Atlantic admits that DIP's recent misfortunes from fires and road construction may not recur and DIP's future financial performance should improve with a reconstructed highway. Atlantic contends the Court should disregard Risher's rebuttal testimony

about the Chalet Bearmouth comparable sale as hearsay based on a copy of a multiple listing report, the accuracy of which Atlantic could not test. Atlantic argues that Risher had nothing to do with the Bearmouth sale and could not testify to its particulars, and concludes that the Bearmouth sale is "rank speculation". Atlantic asks that it be found fully secured by the land, building and going concern valuation.

DISCUSSION

The Court begins by addressing the credibility of the witnesses and Debtor's contention that Stevens' valuation opinion was "bought and paid for" and not credible or entitled to any weight. It is the Court's task to determine the credibility of the witnesses, and after having observed Stevens' demeanor while testifying under oath and subject to cross examination, and reviewing his work product and credentials, the Court finds that Stevens was a credible witness. *In re Taylor*, 514 F.2d 1370, 1373-74 (9th Cir. 1975); *see also Casey v. Kasal*, 223 B.R. 879, 886 (E.D. Pa. 1998). The problems with Stevens' valuation opinion were caused not by his credibility or methodology, but rather the information or lack of information provided to him by both Kingsbury and Atlantic.

Stevens admitted that he was not made aware that Atlantic's security may not include certain assets at the Sula Store property which are subject to other security interests. Atlantic contended in its pleadings that Atlantic has a prior lien over other creditors' liens in FF&E, and that creditors with priority liens should look to their other security before Atlantic's, but Atlantic never filed a Proof of Claim listing its security[21]. Further, Atlantic did not initiate adversary

[21]Indeed, the record lacks any documentation of the terms of the loans underlying Atlantic's claim.

proceedings required to determine the priority of its lien versus other lienholders, or to pursue its claim seeking marshaling of assets. *See, e.g., In re Murdock*, 10 Mont. B.R. 178 (Bankr. D. Mont. 1991). Stevens readily admitted that he was not told that the tank, canopy and pumps or other assets may be security for other creditors, and that occupancy rate can affect income. Such admissions may require downward adjustment of Stevens' appraisal value, but does not undermine Stevens' credibility or methodology.

Turning to Kingsbury's credibility, the Court notes that both Jourdonnais, upon whose appraisal the DIP admits it relies, and Stevens testified that Kingsbury failed to comply with their requests for information about FF&E. Stevens testified that Kingsbury gave him incorrect information about the scope of the utility hookups for some of the cabins, with the result that Stevens' value of the RV site hookups may incorrectly reflect utilities which are not installed for some sites. However, this Court is not inclined to reward the DIP for Kingsbury's failure to cooperate with or for providing incorrect information to appraisers hired by its secured lender.

Kingsbury valued the real property at $500,000, which the DIP argues is supported by Ex. A if the value of cabins and cottages is deducted from Ex. A's $550,000 valuation. This Court discussed the standard for assigning weight to a debtor's testimony of the value of his property in *In re Hungerford*, 19 Mont. B.R. 118-19 (Bankr. D. Mont. 2001):

> While a debtor's estimate of value may be acceptable in certain cases, the Court may give little weight to the opinion if not based upon sufficient facts. *In re Schenk*, 67 B.R. 137, 140 (Bankr. Mont. 1986). The determination of the weight to be given expert testimony or evidence is a matter within the discretion of the trier of fact – which in a nonjury proceeding like the instant case is the bankruptcy court. *Fox v. Dannenberg*, 906 F.2d 1253, 1256 (8th Cir. 1990); *Arkwright Mutual Insurance Co. v. Gwinner Oil Inc.*, 125 F.3d 1176, 1183 (8th Cir. 1997); Barry Russell, *Bankruptcy Evidence Manual*, 2000 Ed., § 702.2. In this contested matter, the trial court acts as a factfinder as well as a gatekeeper. In such instances the

> court's discretion includes the weight to be accorded to the evidence. 4 Joseph M. McLaughlin, *Weinstein's Federal Evidence* § 702.05[2][a] (2nd ed. 2000).

In re Schmitt, 19 Mont. B.R. 57, 75 (Bankr. D. Mont. 2002), quoting *Hungerford.*

Kingsbury testified that his $500,000 value opinion is supported by Jourdonnais in Ex. A because he claimed Jourdonnais included projected income from 4 cabins and cottages which are not part of Atlantic's security. Kingsbury's testimony is flatly contradicted by DIP's own exhibit, Ex. A, which specifically states that his $550,000 value opinion is for real estate only and does not include FF&E or going concern business value. Ex. A, cover letter & p. 25 ("4 are portable and are not part of appraisal"). Ex. C omitted any valuation for the nonpermanent cabins and cottages. Further, the evidence shows that rental income from cabins and cottages which may be lost would be made up for to some extent by use of the same sites as RV site rentals.

Next, Kingsbury's reliance on Ex. A must take into account Jourdonnais' statement in Ex. A, p. 36, adjusting sales by 5% annually to reflect market conditions.[22] As noted above in footnote 14 above, the confirmation hearing commenced more than 13 months after the effective date of Jourdonnais' appraisal of March 25, 2004, and so 5% must be added to Jourdonnais' $550,000 valuation of the Sula Store under the analysis of DIP's own Ex. A, resulting in a value on March 25, 2005, of $577,500. Such an adjustment must be made because this Court has long held that the valuation of collateral for purposes of fixing a claim must be at or near the time of

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[22]Ex. A states in its section on "Market Conditions": "The market for commercial buildings along state highways has been active in the past several years with property values escalating at rates between 2% to 5% annually based upon discussions with market participants. By the dataset, this cannot be quantified by available market data. However, I have adjusted the sales on the basis of 5% per annum."

confirmation. *In re Barnes*, 14 Mont. B.R. 187, 190-91 (Bankr. D. Mont. 1995); *In re Rivers*, 10 Mont. B.R. 210, 211 (Bankr. D. Mont. 1991). Stevens' appraisal is more recent and shows that market appreciation rates now run from 10% to 25% per year, Ex. C, p. 14, and Stevens employed an overall appreciation rate of 10%. Applying the 10% low end of Stevens' more recent range of market appreciation to Jourdonnais' valuation results in a market value at or near the time of confirmation of $605,000. Because Jourdonnais admitted, Ex. A, p. 36, that the market appreciation could not at that time be quantified by available market data, the Court deems it appropriate to apply Stevens' more recent 10% appreciation rate for the Sula Store, which is located in the high-demand Bitterroot Valley.

Kingsbury's $500,000 not only contradicts DIP's own Ex. A, and fails to take into account annual market appreciation, it also is contradicted by the DIP's own 2004 financial statement filed with its supplement to Disclosure Statement which lists $522,347 in "new construction" alone among fixed assets, along with another $289,000 worth of land, buildings and improvements. Kingsbury values the property at $500,000 in 2005 which the Debtor purchased for $450,000 in 1998 and made $500,000 in improvements thereafter, including an environmental cleanup.

Upon consideration of Ex. A and C and after observing Kingsbury, Jourdonnais, Stevens and Risher each testify under oath at hearing, the Court assigns greater weight to Jourdonnais' and Stevens' testimony, and little weight to Risher or Kingsbury. Simply put, the Court assigns no probative weight to Kingsbury's $500,000 valuation, as it contradicts DIP's own Ex. A and financial statements, and Kingsbury failed to cooperate with the appraisers.

Risher is not a licensed appraiser, and his testimony about the Chalet Bearmouth sale for

$384,000 on June 24, 2004, has little probative value. First, the DIP does not contend that the Sula Store is worth $384,000. Kingsbury himself valued the Sula Store property at $500,000. Chalet Bearmouth is located on different highway, on a different river, in a different valley, in a different County than the Sula Store property, and Risher's rebuttal testimony does not provide any adjustments for those factors or size, condition, quality and amenities. The DIP argues that Stevens' made inappropriate adjustments to comparable sales based on unfounded assumptions. But DIP's own evidence, Ex. A at pp. 35-38, recognized that adjustments are appropriate when warranted under the Sales Comparison Approach for condition, size, quality and amenities, and Jourdonnais applied an adjustment for non-real estate assets. Without consideration of or adjustment based upon such factors, Risher's testimony about the sale of the Chalet Bearmouth is incomplete, and in this Court's view entitled to no probative weight.

Stevens' valuation suffers from the lack of information, or incorrect information, with which he was provided. Competing liens may exist on certain FF&E, the priority of which cannot be reconciled based on the record. Stevens admitted that such things as gas pumps, tank, canopy and islands which are subject to other security interests should not have been included in his appraisal. As a result, the Court declines to include in its valuation the $170,000 estimated value of a "going concern" business enterprise which Stevens included in Ex. C, because it is unclear what comprises the "going concern" that secures Atlantic's claim. He also admitted that the lack of utilities at RV site hookups would result in a reduction of rental revenue, and he admitted that a lower vacancy rate would reduce revenues and valuation.

Taking all these factors into consideration, the Court fixes the value of Atlantic's security at the Sula Store property at the sum of $605,000, which both reflects an appropriate market

appreciation of the value Jourdonnais concluded in Ex. A to reflect the passage of time, and to reduce from Stevens' $675,000 valuation amounts caused by Kingsbury's misinformation and failure to cooperate, and exclusion of the value of assets which have not been shown to be Atlantic's collateral.

Confirmation & Cram Down.

Bankruptcy Courts have an affirmative duty to ensure that the Plan satisfies all 11 U.S.C. § 1129 requirements for confirmation. *In re Ambanc La Mesa Ltd. Partnership*, 115 F.3d 650, 653 (9th Cir. 1997), *cert. denied*, 522 U.S. 1110, 118 S.Ct. 1039, 140 L.Ed.2d 105 (1998); *In re L & J Anaheim Assoc.*, 995 F.2d 940, 942 (9th Cir.1993); *In re McKay*, 14 Mont. B.R. 296, 299-300 (Bankr. D. Mont. 1995), quoting *In re Roberts Rocky Mountain Equipment Co., Inc.*, 76 B.R. 784, 789, 4 Mont. B.R. 230, 238 (Bankr. D. Mont. 1987). Section § 1129(a) sets forth thirteen requirements to be met before the bankruptcy court may confirm a Plan. *Ambanc*, 115 F.3d at 653. The Court must confirm a Chapter 11 debtor's plan of reorganization if the debtor proves by a preponderance of the evidence either (1) that the Plan satisfies all thirteen requirements of 11 U.S.C. § 1129(a), or (2) if the only condition not satisfied is the eighth requirement, 11 U.S.C. § 1129(a)(8), the Plan satisfies the "cramdown" alternative to this condition found in 11 U.S.C. § 1129(b), which requires that the Plan "does not discriminate unfairly" against and "is fair and equitable" towards each impaired class that has not accepted the Plan. *Ambanc*, 115 F.3d at 653; *In re Arnold and Baker Farms*, 177 B.R. 648 (9th Cir. BAP 1994), *aff'd*, 85 F.3d 1415 (9th Cir.1996), *cert. denied*, 519 U.S. 1054, 117 S.Ct. 681, 136 L.Ed.2d 607 (1997); *see also In re Red Lodge Country Club Estates Joint Venture*, 13 Mont. B.R. 172, 181 (Bankr. D. Mont. 1994). In the instant case § 1129(a)(8) is not satisfied because Atlantic is impaired and rejects the DIP's

Plan, so Debtor must satisfy the cramdown.

The BAP in *In re Yett*, 306 B.R. 287, 290-91 (9th Cir. BAP 2004) discusses the terms of art "cramdown" and "cram down":

> [T]hey refer to the modification of the rights of a secured creditor over its objection. As noted by a leading scholar:
>
> > In many cases filed under Chapter 13 of the Bankruptcy Code, the debtor wants to keep her car or truck and modify the terms of her car note in a manner that is not acceptable to the lender. And, in many Chapter 11 business cases, the debtor wants to keep its equipment or building and modify the terms of its secured loan in a manner that is not acceptable to the lender. A bankruptcy court can confirm a Chapter 11, 12, or 13 plan that modifies the rights of a secured creditor without the consent of that creditor. In other words, the plan can be "crammed down" over the objection of the secured creditor.
> >
> > ....
> >
> > [T]here are two separate valuations involved in the cram down of a secured claim. First, the court must determine the value of the creditor's collateral. Second, the court must determine the value of the deferred payments proposed by the plan to determine whether the present value of such payments at least equals the value of the collateral.
> >
> > ....
> >
> > The cram down of a secured claim involves not only section 506 [providing that creditor's secured claim is limited to the value of the collateral], but also section 1129(b)(1), section 1222(b)(2), or section 1322(b)(2), which permit a Chapter 11, 12, or 13 plan to "impair" or "modify" the rights of holders of secured claims. Any plan impairment or modification must be confirmed by the bankruptcy judge. In approving such a change over the objection of the affected secured creditor, the court must find that the requirements of sections 1129(b)(2)(A), 1225(a)(5)(B)(ii), or 1325(a)(5)(B)(ii), generally referred to as the cram down provisions, have been satisfied.
> >
> > ....
> >
> > [T]he courts and commentators have generally treated the question of

> how the cram down interest rate should be determined as a question that is answered the same in Chapter 11, 12, and 13 cases. Note the italicized phrase, "value, as of the effective date of the plan," in each of these sections. Each of these provisions requires that a secured creditor who is not either paid in full or permitted to repossess must receive the present equivalent value of its secured claim.
>
> David G. Epstein, *Don't Go and Do Something Rash about Cram Down Interest Rates*, 49 Ala. L.Rev. 435, 439-442 (1998)(footnotes omitted).

Applying the above, the first task is to fix the value of Atlantic's collateral to determine under § 506(a) the extent that Atlantic's claim is secured by value of property on which its lien is fixed, with the remainder considered unsecured. *Hungerford*, 19 Mont. B.R. at 111; *In re Stratton*, 18 Mont. B.R. 293, 296 (Bankr. D. Mont. 2000). In *Hungerford*, this Court noted that the proper value for cramdown in a Chapter 13 case is "the cost the debtor would incur to obtain a like asset for the same proposed use." 19 Mont. B.R. at 111; *Stratton*, 18 Mont. B.R. at 300, quoting *Associates Commercial Corp. v. Rash*, 520 U.S. 953, 965, 117 S.Ct. 1879, 1886, 138 L.Ed.2d 148 (1997). The Supreme Court concluded that under § 506(a), where as in the instant case a debtor has opted to retain the collateral and exercise the cramdown option, the value of property retained is the cost a debtor would incur to obtain a like asset for the same proposed use. *Rash*, 520 U.S. at 965, 117 S.Ct. at 1886. The *Rash* standard is used synonymously with the Ninth Circuit's understanding of "fair market value", i.e. the price a willing buyer in the debtor's trade, business, or situation would pay a willing seller to obtain property of like age and condition. *Hungerford*, 19 Mont. B.R. at 111; *Rash*, 520 U.S. at 959 n.2, 117 S.Ct. at 1883-4 n.2; *In re Taffi*, 96 F.3d 1190, 1191-92 (9th Cir. 1996). Cases under both Chapter 11 and Chapter 13 are subject to the same § 506(a) analysis above in determining the value of a creditor's collateral, so the *Rash* standard for cram down applies to the instant Chapter 11 case in

determining the value of Atlantic's security for cramdown purposes.

Applying this standard to the $605,000 valuation concluded above, the DIP listed Atlantic on Schedule D as having a secured claim with no unsecured portion, but now contends that it is undersecured. Subtracting from this Court's $605,000 valuation the amount of the prior liens against the Sula Store according to DIP's Schedules and/or Proofs of Claim filed, i.e., Ravalli County's property tax claim of $15,105 and Farmers State Bank's $387,068 from Proof of Claim No. 5, which combined total is $402,173, the Court finds that Atlantic's secured claim for cram down purposes under § 506(a) is $202,827, having been determined in light of the purpose of the valuation and of the proposed use of such property, after notice and a hearing, and its unsecured claim is $89,156.

Fair and Equitable – § 1129(b)(2)(A).

The § 1129(b)(2) cramdown provision specifies that a fair and equitable plan provide one of three alternatives for the holders of secured claims: (A)(i)(I) that the holders of such claims retain the liens securing such claims, whether the property subject to such liens is retained by the debtor or transferred to another entity, to the extent of the allowed amount of such claims; and (II) that each holder of a claim of such class receive on account of such claim deferred cash payments totaling at least the allowed amount of such claim, of a value, as of the effective date of the plan, of at least the value of such holder's interest in the estate's interest in such property; or (ii) for the sale, subject to section 363(k) of this title, of any property that is subject to the liens securing such claims, free and clear of such liens, with such liens to attach to the proceeds of such sale, and the treatment of such liens on proceeds under clause (i) or (iii) of this subparagraph; or (iii) for the realization by such holders of the indubitable equivalent of such

claims. *Ambanc*, 115 F.3d at 653; *In re Boulders on the River*, 164 B.R. 99, 105 (9th Cir. BAP 1994). The issue in the instant case is § 1129(b)(2)(A)(i)(II); that is whether "each holder of a claim of such class receive on account of such claim deferred cash payments totaling at least the allowed amount of such claim, of a value, as of the effective date of the plan, of at least the value of such holder's interest in the estate's interest in such property." § 1129(b)(2)(A)(i)(II); *McKay*, 14 Mont. B.R. at 303.

Atlantic's secured claim determined under § 506(a) above is $202,827. The attachment to DIP's Disclosure Statement showing annual payments states Atlantic's claim at $291,983 and reflects payments through 2009 and thereafter. The Plan, Article III, provides for annual payments to Atlantic over 20 years, in the absence of a § 1111(b) election, with interest at the rate of 1.25% over prime. Over 20 years such payments under the annual payments attachment to the DIP's Disclosure Statement total $231,000, by the Court's calculation. Such an amount does not pay the amount of Atlantic's claim on the annual payments attachment and Schedule D, $291,983, and the DIP offered no expert testimony or other evidence that the annual payments would pay Atlantic's secured claim in the allowed amount of $202,827, with interest.

Neither did the DIP offer any testimony or evidence supporting its proposed interest rate and 20 year term. The BAP in *Boulders on the River*, 164 B.R. at 105, noted that the Ninth Circuit applies the "formula rate" approach for determining the interest payable on the deferred payment of an obligation under the cramdown. *See also In re Fowler*, 903 F.2d 694, 697 (9th Cir. 1990); *In re Camino Real*, 818 F.2d 1503, 1508 (9th Cir. 1987). Under this approach the court starts with a base rate and adds a risk factor based on the risk of default and the nature of the security. *Boulders on the River*, 164 B.R. at 105; *In re Fowler*, 903 F.2d at 697. The interest rate

determination is to be made on a case-by-case basis. *Boulders on the River*, 164 B.R. at 105; *In re Camino Real*, 818 F.2d at 1508. The Court appreciates the U. S. Supreme Court's plurality decision in *Till v. SCS Credit Corp.*, 541 U.S. 465, 484-85, 124 S.Ct. 1951, 1964 (2004) (a Chapter 13 case), and the statement made by Justice Stevens:

> Justice SCALIA identifies four "relevant factors bearing on risk premium[:] (1) the probability of plan failure; (2) the rate of collateral depreciation; (3) the liquidity of the collateral market; and (4) the administrative expenses of enforcement." Post, at 1973. In our view, any information debtors have about any of these factors is likely to be included in their bankruptcy filings, while the remaining information will be far more accessible to creditors (who must collect information about their lending markets to remain competitive) than to individual debtors (whose only experience with those markets might be the single loan at issue in the case). Thus, the formula approach, which begins with a concededly low estimate of the appropriate interest rate and requires the creditor to present evidence supporting a higher rate, places the evidentiary burden on the more knowledgeable party, thereby facilitating more accurate calculation of the appropriate interest rate.
>
> If the rather sketchy data uncovered by the dissent support an argument that Chapter 13 of the Bankruptcy Code should mandate application of the presumptive contract rate approach (rather than merely an argument that bankruptcy judges should exercise greater caution before approving debt adjustment plans), those data should be forwarded to Congress. We are not persuaded, however, that the data undermine our interpretation of the statutory scheme Congress has enacted.

Till, 541 U.S. at 484-85, 124 S.Ct. 1964-65. As *Till* involves a 4-4-1 decision by the Justices, and given the lack of a consensus on a legal rationale by the Justices, *Till*, however, produces no majority rule of law and results in no binding precedent. "[A]n affirmance by an equally divided court is as between the parties a conclusive determination and adjudication of the matter adjudged, but the principles of law involved not having been agreed upon by a majority of the court sitting prevents the case from becoming an authority for the determination of other cases either in [the Supreme Court] or in inferior courts." *In re Cook*, 322 B.R. 336, 343 (Bankr. N.D.

Ohio 2005), *citing Hertz v. Woodman*, 218 U.S. 205, 213-14, 30 S.Ct. 621, 54 L.Ed. 1001 (1910). Consequently given the burden of proof established in the 9th Circuit Court of Appeals in *Ambanc*, 115 F.3d at 653, the Debtor must satisfy the requirements for confirmation and the creditor is not required to establish the four relevant factors bearing on risk premium which is to be added to the prime rate. Certainly the creditor may provide evidence to the Court to refute the Debtor's proof and to support a higher risk premium. As noted above, the formula approach has been used in this District since the late 1980's.

With respect to the interest rate no expert testimony or other evidence was offered by the DIP at the confirmation hearing of the appropriate risk factor other than the Plan's bald 1.25% statement, or even of the prime rate on that day.[23] Likewise there was no expert testimony or other evidence offered supporting the Plan's 20 year term for Atlantic. Apparently the DIP's position is that the statements in its Plan are all the evidence required, but DIP is mistaken.

Where a debtor does not offer evidence in support of interest rate and term it runs the risk that confirmation will be denied and the Chapter 11 case dismissed. *See, e.g.*, *In re Mohr*, 5 Mont. B.R. 241, 248-49 (Bankr. D. Mont. 1987). In a 1993 Chapter 11 case, *In re Brummer*, 12 Mont. 219, 224 (Bankr. D. Mont. 1993), this Court concluded from the evidence that a commercial lender would not make a 100% leveraged loan over a 20 year term. Courts have stated that in general a plan is not fair and equitable with respect for a secured lender when the plan unduly shifts the risks of a successful reorganization to those creditors. *In re Crown Oil, Inc.*, 16 Mont. B.R. at 534, 539 (Bankr. D. Mont. 1998) (citing cases). Based on the risk of

[23] The prime rate of interest on the date of the confirmation hearing was 6%. The prime rate of interest was 5% when Debtor filed its proposed plan. Effective June 30, 2005, the prime rate was increased to 6.25%.

default, which this Court deems high in this case, and the nature of the security, this Court finds no support for the 1.25% above prime risk factor in the record, or at law. *Boulders on the River*, 164 B.R. at 105; *In re Fowler*, 903 F.2d at 697. The DIP's Plan already reduces its initial annual payments by 30% to restore working capital, but the 2004 financial statement shows another reason for the reduction – a mere $7 net profit after debt service and depreciation. The claims reflect years of unpaid property taxes, which increases the risk. *Brummer*, 12 Mont. at 224.

The Court must consider the Plan in the context of the rights of objecting creditors and the particular facts and circumstances of the debtor's financial plight in determining whether a plan is fair and equitable under § 1129(b)(2). *Brummer*, 12 Mont. at 224, quoting *Sandy Ridge Dev. Corp. v. Louisiana Nat'l Bank (Matter of Sandy Ridge Dev. Corp.)*, 881 F.2d 1346, 1352 (5th Cir. 1989) ("[T]echnical compliance with the requirements of section 1129(b)(2) does not assure that the plan is fair and equitable. Instead, this section merely sets minimal standards ....") (other citations omitted). Based upon the complete lack of evidence supporting its proposed interest rate and plan term, this Court finds and concludes that DIP's Plan fails the "fair and equitable requirement" of § 1129(b)(2)(A)(i)(II). *Boulders on the River*, 164 B.R. at 105; *In re Fowler*, 903 F.2d at 697.

Feasibility – § 1129(a)(11).

This Court is not required to determine that future commercial success for the reorganized DIP is inevitable in order to find that a reorganization plan in Chapter 11 is feasible. *See In re WCI Cable, Inc.*, 282 B.R. 457, 486 (Bankr. D. Ore. 2002).

> "Guaranteed success in the stiff winds of commerce without the protection of the Code is not the standard under § 1129(a)(11). Most debtors emerge from reorganization with a significant handicap. But a plan based on impractical or

> visionary expectations cannot be confirmed.... All that is required is that there be reasonable assurance of commercial viability." *In re The Prudential Energy Co.*, 58 B.R. 857, 862 (Bankr.S.D.N.Y.1986).

WCI Cable, 282 B.R. at 486; *In re Acequia, Inc.*, 787 F.2d 1352, 1364 (9th Cir.1986); *In re Pizza of Hawaii, Inc.*, 761 F.2d 1374, 1382 (9th Cir.1985) ("The purpose of section 1129(a)(11) is to prevent confirmation of visionary schemes which promise creditors and equity security holders more under a proposed plan than the debtor can possibly attain after confirmation."); *see also In re Sagewood Manor Assoc. Ltd. Partnership*, 223 B.R. 756, 762-63 (Bankr.D.Nev.1998) ("While a reviewing court must examine 'the totality of the circumstances' in order to determine whether the plan fulfills the requirements of § 1129(a)(11), ... only 'a relatively low threshold of proof [is] necessary to satisfy the feasibility requirement.' ... The key element of feasibility is whether there exists a reasonable probability that the provisions of the plan of reorganization can be performed."). Factors that the court should consider in evaluating evidence as to feasibility include "(1) the adequacy of the financial structure; (2) the earning power of the business; (3) economic conditions; and (4) the ability of management." *WCI Cable*, 282 B.R. at 486; *In re Agawam Creative Marketing Assoc. Inc.*, 63 B.R. 612, 619-20 (Bankr.D.Mass.1986) *quoting from In re Merrimack Valley Oil Co., Inc.*, 32 B.R. 485, 488 (Bankr.D.Mass.1983).

The burden of proving feasibility is on the DIP. *In re Soo*, 15 Mont. B.R. 159, 163 (Bankr. D. Mont. 1996), citing *In re Martin*, 66 B.R. 921, 925, 3 Mont. B.R. 244 (1986); *Brummer*, 12 Mont. B.R. at 225. A debtor must prove feasibility by more than mere assertion, it must bring forth evidence, including necessary expert testimony, of the likely success of debtor's plan. *Soo*, 15 Mont. B.R. at 162; *Martin*, 66 B.R. at 926. When a Chapter 11 Plan contemplates funding plan payments from operating revenues, past and present financial records are probative

of feasibility, and speculative, conjectural, or unrealistic predictions cannot be used to predict financial progress. *Mckay*, 14 Mont. B.R. at 308; *Brummer*, 12 Mont. B.R. at 226, quoting *In re Hobble-Diamond*, 89 B.R. 856, 858 (Bankr. D. Mont. 1991). Factual support must be shown for the Debtor's projections." *Brummer*, 12 Mont. B.R. at 226.

Applying the above standards to the instant case, after reviewing the totality of the circumstances this Court finds and concludes that the DIP's failed its burden to satisfy the feasibility requirement of § 1129(a)(11), and that there is no reasonable probability that the provisions of the Plan can be performed. Already, DIP's 2004 financial statement attached to its supplement to Disclosure Statement shows that its sales of $568,297 fall far short of its projected 2004 sales of $600,000, thus disproving their projected annual 7% increase in sales. Its 2004 expenses came in just under the projections, but the 2004 financial statement shows a $7 net profit after (reduced) nominal payments, without including the members' $42,000 projected annual draw. If the members take any draw, DIP's cash flows are hopelessly in the red.

Absolute Priority Rule – § 1129(b)(2)(B).

Atlantic objects that DIP's Plan violates the "absolute priority rule" at § 1129(b)(2)(B) which provides that with respect to a class of unsecured claims –

> (i) the plan provides that each holder of a claim of such class receive or retain on account of such claim property of a value, as of the effective date of the plan, equal to the allowed amount of such claim; or
> (ii) the holder of any claim or interest that is junior to the claims of such class will not receive or retain under the plan on account of such junior claim or interest any property.

Article III of DIP's Plan provides at page 5 that the members' equity interest will be retained, but unsecured creditors in Class 5 will receive no payments until a sinking fund is

established 6 years after the effective date, and then Class 5.2, in which Atlantic's unsecured claim determined above in the sum of $89,156 is classified, will be paid only 50% without interest. This Court construed "absolute priority" in *Brummer*, 12 Mont. B.R. at 222, *citing* 5 Collier on Bankruptcy, ¶ 1125.02 at 1125.8.1 (15th ed.), to mean: "Beginning with the topmost class of claims against the Debtor, each class in descending rank must receive full and complete compensation for the rights surrendered before the next class below may properly participate." By retaining the members' equity while paying Atlantic and other Class 5.2 unsecured claims only 50% of their claims, without interest and after 6 years from the effective date, DIP's Plan violates the absolute priority rule and cannot be confirmed.

Having determined that the DIP's Plan fails to satisfy the requirements of § 1129(a)(11) and § 1129(b)(2), the next step is to determine the appropriate disposition of this case. Denial of confirmation is cause for dismissal or conversion to Chapter 7, whichever is in the best interests of creditors and the estate, under 11 U.S.C. § 1112(b). This case has been pending since June 18, 2004, more than a year. Valuation was not originally at issue since Atlantic was listed on Schedule D as undisputed and with no unsecured portion of its claim. DIP employed an improper procedure to raise the issue of valuation of Atlantic's security until January 2005 when it filed its motion for valuation, and then after raising the issue of valuation and drawing this case out several months did not procure or offer experts to testify regarding the contested valuation, or in support of DIP's proposed interest rate, term, or feasibility. DIP's lack of evidence on market rate and loan term allows the Court no flexibility under the record to accept its proposed term and interest rate. This Court has repeatedly held that the Court must take the Plan in its entirety as proposed, and cannot write Plans for Debtors. *Mohr*, 5 Mont. B.R. at 249 n.2, citing *Janssen*

Charolais Ranch, Inc., 73 B.R. 125, 128, 4 Mont. B.R. 290, 297 (Bankr. D. Mont. 1987). DIP's liquidation analysis attached to its Disclosure Statement shows $0 equity for creditors. The Court concludes that cause exists to dismiss this case under § 1112(b), and that dismissal is in the best interests of creditors and the estate.

CONCLUSIONS OF LAW

1. This Court has jurisdiction of this Chapter 11 bankruptcy case under 28 U.S.C. § 1334(a).

2. The DIP's motion for valuation of Atlantic's security and confirmation of the DIP's Chapter 11 Plan of Reorganization are core proceedings under 28 U.S.C. § 157(b)(2)(K), (L), and (O).

3. The valuation of Atlantic's security and allowed secured claim pursuant to 11 U.S.C. § 506(a) is fixed in the amount of $605,000, having been determined in light of the purpose of the valuation and of the proposed use of such property, after notice and a hearing; and Atlantic's secured claim for cram down purposes under § 506(a) is $202,827 and its unsecured portion is $89,156.

4. DIP's Plan of Reorganization fails to satisfy the "fair and equitable" confirmation requirement of 11 U.S.C. § 1129(b)(2)(A)(i)(II) by failing to provide that Atlantic receive on account of its allowed secured claim the amount of such claim of a value, as of the effective date of the Plan, of the value of Atlantic's interest in the estate's interest in Atlantic's security.

5. DIP's Plan of Reorganization fails to satisfy the feasibility confirmation requirement of 11 U.S.C. § 1129(a)(11)

6. DIP's Plan of Reorganization fails to satisfy the "absolute priority" confirmation

requirement of 11 U.S.C. § 1129(b)(2)(B) because of retention of DIP's members' equity while paying Class 5.2 unsecured creditors 50% of their claims without interest.

7. Cause exists under 11 U.S.C. § 1112(b) to dismiss this Chapter 11 bankruptcy case based upon DIP's failure to satisfy the confirmation requirements of §§ 1129(a)(11), (b)(2)(A)(i)(II) and (b)(2)(B); and dismissal is in the best interests of creditors and the estate.

IT IS ORDERED a separate Order shall be entered in conformity with the above granting in part and denying in part DIP's motion for valuation of Atlantic's security, fixing the valuation of Atlantic's security the Sula Store property at the sum of $605,000 and the amounts of Atlantic's secured claim and unsecured claim for cram down purposes under § 506(a) at $202,827 and $89,156, respectively; sustaining Atlantic's objection to confirmation and denying confirmation of the DIP's Chapter 11 Plan of Reorganization, and dismissing this case.

BY THE COURT

Ralph B. Kirscher

HON. RALPH B. KIRSCHER
U.S. Bankruptcy Judge
United States Bankruptcy Court
District of Montana